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IN FUTURE ISSUES

- Income tax consequences of disaster payments and drought sales
- The problem of non-U.C.C. liens on agricultural collateral

Farm wages are subject to withholding

For tax years beginning before 1990, farmers and their employees had the option of withholding income taxes from the employee's wages or not withholding. Section 7631(a) of the Omnibus Budget Reconciliation Act of 1989 amended I.R.C. 3401(a)(2) by removing the option to *not* withhold if the wages are subject to FICA taxes. Consequently, beginning in 1990, many farm wages are subject to income tax withholding.

Farm wages that are not subject to FICA tax and therefore are not subject to income tax withholding include the following:

(1) Wages paid to any employee so long as the wages paid to that employee do not exceed $150, *and* so long as the total wages paid by the employer to all employees does not exceed $2,500. Total wages of $2,500 or more does not trigger the withholding requirement if all of the following conditions are met: (a) the employee is employed as a hand harvest laborer and is paid on a piece rate basis in an operation which has been, and is customarily and generally recognized as having been, paid on a piece rate basis in the region of employment; (b) the employee commutes daily from his permanent residence to the farm on which he is employed, and (c) the employee has been employed in agriculture less than 13 weeks during the preceding calendar year. I.R.C. 3121(a)(8)(B).

(2) All wages paid to the employer's child who is under the age of 18 years. If a partnership is the employer, the employee must be a child of all the partners for this exception to apply. I.R.C. 3121(b)(3).

(3) Remuneration paid in any medium other than cash for agricultural labor. I.R.C. 3121(a)(8(A).

Note that if the farm business is incorporated, wages paid to the owner-operator are subject to the above rules. However, if the farm business is in a partnership, the partner's draw from the partnership is not subject to income tax withholding. Rev. Rul. 69-184, 1969-1 C.B. 256.

The withholding rules require the employee to fill out a W-4 and give it to the employer. The withholding tables are not published in Circular A, *Agricultural Employers Tax Guide,* so farmers must use Circular, *Employers Tax Guide* to determine the amount of income tax to withhold. The withheld income taxes must be deposited at the end of any month in which the accumulated income tax withholding and FICA taxes equal or exceed $500.

– Philip E. Harris, Associate Professor, University of Wisconsin-Madison

Zajac vacated

On December 7, 1989, barely two months after the filing of the panel decision in *Zajac v. Federal Land Bank of St. Paul,* 887 F.2d 844 (8th Cir. 1989), the opinion was vacated pending a rehearing *en banc.* (1989 U.S. App. LEXIS 18809). The panel had found that the Agricultural Credit Act of 1987 implied a private right of action against Farm Credit System lenders to enforce, through injunctive relief, the procedural requirements of the debt restructuring provisions of the Act. *See* 7 Agric. L. Update 1 (Nov. 1989).

The vacating of the panel opinion in *Zajac* leaves *Harper v. Federal Land Bank of Spokane,* 878 F.2d 1172 (9th Cir. 1989), *cert. denied,* 58 U.S.L.W. 3468 (U.S. Jan. 22, 1990), as the only federal court of appeals ruling on the issue of whether FCS borrowers have an implied cause of action to enforce the provisions of the 1987 Act. In *Harper,* the Ninth Circuit held that there was no implied cause of action. *See,* 7 Agric. L. Update 1 (Aug. 1989).

Oral arguments in the rehearing *en banc* in *Zajac* were held on January 19, 1990. The full court's opinion should be forthcoming in the next couple of months.

Implied cause of action litigation involving the FCS "borrowers' rights" provisions of the 1987 Act has been prolific. Since the filing of the Ninth Circuit's opinion in *Harper,* decisions on the issue include the following: *Walker v. Federal Land Bank of St. Louis,* 726 F. Supp. 211 (C.D. Ill. 1989)(no implied cause of action); *Renick Bros., Inc. v. Federal Land Bank Ass'n of Dodge City,* 721 F. Supp. 1198 (D. Kan. 1989)(no implied cause of action); *Stoppel v. Farm Credit Bank of Wichita,* No. 89- 1221-C (D. Kan. Sept. 26, 1989)(1989 U.S. Dist. LEXIS 11642)(no implied cause of action); *Ochs v. Federal Land Bank of Wichita,* No. 87-4113-R (D. Kan. July 13, 1989)(1989 U.S. Dist. LEXIS 9079)(no implied cause of action); *Penz v. Farm Credit Services,* No. 89-577-C (E.D. Okla. Dec. 6,

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1989)(order granting injunctive relief)(finding an implied cause of action); *Hill v. Farm Credit Bank of St. Louis*, No. N-88-0079-C (E.D. Mo. Dec. 6, 1989) (1989 U.S. Dist. LEXIS 14594) (finding an implied cause of action based on *Zajac); In re: Jarrett Ranches, Inc.*, No. 88-10117 (Bankr. S.D. Aug. 16, 1989) (1989 Bankr. LEXIS 1340), *appeal docketed*, No. CIV-89-1039 (D. S.D. Oct. 6, 1989)(finding an implied cause of action). *See also Wilson v. Federal Land Bank of Wichita*, No. 88-4058-R (D. Kan. Jan. 30, 1989)(1989 U.S. Dist. LEXIS 1558)(no implied cause of action; *Neth v. Federal Land Bank of Jackson*, 717 F. Supp. 1478 (S.D. Ala. 1988)(no implied cause of action); *Martinson v. Federal Land Bank of St. Paul*, No. A2-88-31 (D. N.D. April 21, 1988), *appeal dismissed*, No. 88-5202 (8th Cir. May 5, 1989)(finding an implied cause of action); *Leckband v. Naylor*, 715 F. Supp. 1451 (D. Minn. 1988), *appeal dismissed*, No. 88-5301 (8th Cir. May 5, 1989)(finding an implied cause of action).

– Christopher R. Kelley, National Center for Agricultural Law Research and Information

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Federal Register *in brief*

The following is a selection of matters that have been published in the *Federal Register* from January 3, 1990 to February 2, 1990:

1. USDA; Implementation of the Program Fraud Civil Remedies Act of 1986; proposed rule. 55 Fed. Reg. 636.

2. USDA; Agricultural Marketing Service; Notice of continuation of Federal-State Marketing Improvement Program; invitation for applications; proposals accepted until 9/90. 55 Fed. Reg. 1686.

3. EPA; Endangered Species Protection Program; US Fish and Wildlife Service Biological Opinion on Selected Pesticides; notice of availability of document; 55 Fed. Reg. 1168.

4. CCC; Peanut warehouse storage loans and handler operations for the 1986 through 1990 crops; final rule; effective date 1/16/90. 55 Fed. Reg. 1383; 1385.

5. ASCS; CCC; Criteria used to determine a "farm," payment limitation provisions; foreign person provisions; interim rule; effective date 1/17/90. 55 Fed. Reg. 1557.

6. FMHA; Adverse decisions and administrative appeals; hearing officer's decision; review; final rule; effective date 2/16/90. 55 Fed. Reg. 1576. *– Linda Grim McCormick, AALA Editor, Toney, AL*

Errors in Farmer's Tax Guide

The 1989 edition of the I.R.S. Publication #225, *Farmer's Tax Guide*, has two errors that the I.R.S. will correct with Notices in the near future.

Farmer status for estimated taxes

One error is in the definition of farm gross income for purposes of the ⅔ test that is used to determine if a taxpayer must make estimated tax payments. The ⅔ test is discussed on page 4 of the publication. Under that test, if ⅔ of a taxpayer's adjusted gross income is from farming, the taxpayer can avoid the penalty for under payment of estimated taxes by either making one estimated payment for the tax year by January 15 of the year following the tax year, or by filing the tax return and paying the taxes due by March 1 of the year following the tax year. In that discussion, the reader is referred to Chapter 4 for the definition of gross income from farming. However, the definition of gross income in Chapter 4 *excludes* gains from sales of livestock held for draft, breeding, sport, or dairy purposes. That is not the correct definition for purposes of the ⅔ test for the estimated tax exemption. For purposes of the ⅔ test, gains from sales of livestock held for draft, breeding, sport, or dairy purposes should be *included* in farm gross income.

Disaster payments received in 1989

The second error is in the discussion of crop insurance and disaster payments on page 11 of the publication. In that discussion, the publication says that payments received under Title I of of the Disaster Assistance Act of 1989 can be treated as insurance payments. In fact, the amendment to the Internal Revenue Code that would have allowed that treatment was stripped out of the Omnibus Reconciliation Act of 1989 and has not been reintroduced in any other legislation. The I.R.S. says it is now unlikely that Congress will amend the Code to allow the payments received under the Disaster Assistance Act of 1989 to be reported on the 1990 return.

Note that payments under Title II of the Disaster Assistance Act of 1988 could be reported on the 1989 tax return if they were received in 1988 and the taxpayer qualified for the I.R.C. 451(d) election. However, if payments under Title II of the Disaster Assistance Act of 1988 were received in 1989, they cannot be reported on the 1990 return because I.R.C. 451(d) allows the taxpayer to postpone reporting only until the year *after* the crops were destroyed or damaged.

To sum up, *any* disaster payment received in 1989 is *ineligible* for the I.R.C. 451(d) election to postpone reporting by one year.

– Philip E. Harris, Associate Professor, University of Wisconsin-Madison

State Roundup

PENNSYLVANIA. *Stray voltage*. In the case of *Slater v. Pennsylvania Power Co.*, 557 A.2d 368 (Pa. Super. 1989), the Slaters, a dairy family, filed a tort action against an electric utility for economic injuries. The Slaters had noticed in their herd a decline in milk production, health problems, and unusual behavior. Upon investigation, stray voltage was found. The utility suggested several changes to be made at the Slaters' expense to solve the problem, to no avail. Subsequently, the Slaters' electrician disconnected a ground wire that ran from the utility's pole; the stray electricity disappeared. When the wire was reconnected with modification, the stray voltage problem did not recur.

The jury awarded the Slaters damages of $81,374.41. The utility appealed, arguing that it was entitled to judgment n.o.v., that there were errors in the jury charge, and that the proof of damages was inadequate.

At trial, the Slaters argued that the utility was negligent in supplying power to their farm and in its failure to immediately reduce or eliminate the stray

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Bibliography of law review articles on agricultural law

The following is a listing of recent law review articles relating to agricultural law.

Administrative law

Hamilton, *Legal Issues Arising in Federal Court Appeals of ASCS Decisions Administering Federal Farm Programs*, 12 Hamline L. Rev. 633-648 (1989).

Linden, *An Overview of the Commodity Credit Corporation and the Procedures and Risks of Litigating Against It*, 11 J. Agric. Tax'n & L. 305-330 (1990).

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General

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Williams, *The Qualified Farm Indebtedness Exception to Taxation of Discharged Debt: Making Hay Under TRA*, 50 Mont. L. Rev. 279-311 (1989).

Biotechnology

Wadley, *Regulating Agricultural Biotech Research: An Introductory Perspective*, 12 Hamline L. Rev. 569-588 (1989).

Cooperatives

General

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Baarda, *Farmer Cooperative Equity Conflicts: Judicial Decisions in the 1980s*, 12 Hamline L. Rev. 699-724 (1989).

Taxation

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Equine law

Husband, *How to "Land" a Profit in the Horse Business*, 11 J. Agric. Tax'n & L. 161-169 (1989).

Marsh & Bizzell, *Farm Losses and the Limitations on Activities Not Engaged in for Profit*, 11 J. Agric. Tax'n & L. 291-304 (1990).

Estate planning/divorce

Harl, *The Death Knell for Estate Freezes*, 11 J. Agric. Tax'n & L. 170-180 (1989).

Harl, *Planning to Avoid or Minimize the Generation-Skipping Transfer Tax*, 11 J. Agric. Tax'n & L. 347-356 (1990).

Farm labor

Aliens

Comment, *Overcoming Mootness in the H-2A Temporary Foreign Farmworker Program*, 78 Geo. L.J. 197-230 (1989).

General

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Farmers Home Administration

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Finance and credit

Golann, *Taking ADR to the Bank: Arbitration and Mediation in Financial Services Disputes*, 44 Arb. J. 3-14 (1989).

Harl, *The Future of Agricultural Credit*, 12 Hamline L. Rev. 607-632 (1989).

Forestry

Daughtrey & Burckel, *Is Damage Caused by the Southern Pine Beetle Deductible as a Casualty Loss?*, 11 J. Agric. Tax'n & L. 331-346 (1990).

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Land use planning and farmland preservation techniques

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Thompson, *Purchase of Developments Rights: Ultimate Farmland Preservation Tool?*, 12 Zoning and Plan. L. Rep. 153 (1989).

Pesticides

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Article Two

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– *Drew L. Kershen, Professor of Law, The University of Oklahoma College of Law*

STATE ROUNDUP / CONTINUED FROM 2

voltage. The utility argued that stray electricity is an inherent part of power distribution and presents a problem only when the amount is too great.

The utility conceded at trial that the amount of stray electricity was too great in this case. Based upon the position taken by the Slaters at trial, the jury apparently agreed that the utility was negligent. The appellate court found that that was a reasonable result from the evidence presented. Accordingly, denial of the motion for judgment n.o.v. was proper.

On the issue of proof of economic loss, the appellate court noted that the Slaters had the burden of proving damages by a preponderance of the evidence, but that they needed only to provide the jury with a reasonable amount of information to enable them to estimate damages without resorting to speculation. In this case, proof of economic loss could be established by testimony of the dairy farmer himself, relying on personal knowledge and books and records of the business.

At trial, the Slaters' jury instruction stated that anyone who provides or supplies an inherently dangerous instrumentality, such as the supplier of high-voltage electric current, is required by law to use the highest degree of care practicable to avoid injury to anyone who may lawfully be in the area. This instruction was based on two Pennsylvania cases, *Kintner v. Claverack Rural Electric Cooperative*, 329 Pa. Super. 417, 478 A.2d 858 (1984) and *Schriner v. Pennsylvania Power and Light Co.*, 348 Pa. Super. 177, 501 A.2d 1128 (1985). The utility argued that the highest degree of care applies only to injuries suffered by humans, but did not cite any cases in support of this distinction. The appellate court held that the two cited cases were the law in Pennsylvania and that the standard of care does not vary when the damages consist of property damage rather than personal injury.

– *John C. Becker, Associate Professor, Agricultural Economics, Penn State University*

FARM FLIPS: Restructuring agriculture in the 1990's

by Nels Ackerson

This is the first in a series of comments drawn from a speech entitled, "'FARM FLIPS: New Regimes in Farmland Ownership," delivered at the annual meeting of the American Agricultural Law Association in San Francisco, November 2, 1989. Other comments will appear in future issues of the *Agricultural Law Update*.

Introduction

Farmland ownership is changing. The 1990's will see profound alterations in farmland ownership demographics. Even more fundamentally, the costs and benefits of farmland ownership are changing: in some cases new costs are outstripping tradition benefits. Finally, the very concept of farmland ownership is evolving – in law, economics, and policy.

These changes, some of which have been developing for a long period of time, are not coming to fruition overnight, but their pace may be quickening as we enter the final decade of the century. Traditional perspectives on farmland ownership are inadequate to address the changing realities of the 1990's. Conventional analysis and orthodox transactions must be flipped and reexamined in order to be relevant to today's developments and tomorrow's needs. Innovative lawyers, businessmen, academics, and policymakers are responding with creative thinking and new solutions, institutions, and relationships.

The factors of ***F***inancial relationships, ***A***sset size, ***R***isk management, and ***M***arketplace adaptations will be affected by diverse elements, both inside and outside of agriculture. Participants in restructuring farmland ownership in the 1990's will include: ***F***armers, ***L***enders, ***I***nvestors, ***P***urchasers of farm products, and ***S***uppliers of farm inputs. The first letters of these factors and participants may be combined to form the words: "FARM FLIPS" – hence the name given to these comments and also to the speech delivered by the author on the same subject. The image of "farm flips" also illustrates creative analysis and new institutional arrangements and perspectives on farmland ownership.

The following is a survey of the changing landscape of farmland ownership and a review of policy approaches that have attempted to reverse, alter, or accelerate trends. Subsequent comments will focus on specific currents that appear to be shaping the future of farmland ownership, control, and use.

Nels Ackerson is a partner in the law firm of Sidley & Austin, Washington, D.C.

Farmland ownership in perspective

The 1980's brought unusually large numbers of farmland transfers as a result of economic hardship. The 1990's promise to bring unusually large numbers of farmland transfers as a result of retirement or death. Individuals own substantially all of the farmland in many Midwestern and Plains states where corporate farm ownership is prohibited, and individuals own the vast majority of farms and farmland in other states. In the past few years, the median age of farmers has risen.[1] Therefore, barring surprising increases in life expectancy, more land transfers by reason of retirement or death can be anticipated in the coming years.

The mere passing of land from one generation of farmers to the next would hardly justify a description of fundamental restructuring of farmland ownership. However, other demographic shifts are apparent. Among recent farmland sales nationwide, seventy-one percent of the farms were owner-operated after the sale, while only forty-one percent were owner-operated before the sale. Owner-operators accounted for fifty-seven percent of all reported purchases in 1989 and fifty-six percent of all reported purchases in 1988. On the other hand, the proportion of sales by active farmers who either remained in, retired from, or quit farming has declined. This group accounted for thirty-eight percent of the sales in 1989, down from forty-percent in 1988, and forty-five percent in 1982.[2] Three fourths of recent farmland purchases in Minnesota, for example, were expansion purchases by nearby farmers.[3]

In recent years, average return on assets for farms with gross sales in excess of $500,000 per year has been as high as twenty percent, while smaller farms have had substantially lower returns, ranging rapidly downward to negative returns for farms with less than $100,000 annual sales.[4] Recent years have also been times of unusual volatility in farmland incomes and land values.[5] A high percentage of recent farmland acquisitions have been for cash, reflecting strengthened financial positions of farmers – particularly larger farming operations – who survived the economic reshuffling of the last six years.[6]

Those larger, cash-strong farming operations will be in strong competitive positions to bid for farms that come on the market in coming years. Purchasers of farmland are likely to be larger, better financed, and more technologically sophisticated than the sellers.

The demographic patterns discussed above suggest that in the 1990's relatively large numbers of farms and farmland acreage will be transferred during a period of diversification in finance, increasing economies of scale, vertical integration in some sectors, deployment of new technology, reform of domestic and international farm supports, and changing market preferences. Revolutionary structural change in agriculture is possible.[7]

Recent developments in genetic research illustrate the potential for rapidly changing roles of farmland ownership. A leading newspaper recently carried the headline, "Agricultural Alchemists Dispense with Farms." The article described a concept of genetically engineered cultures that would use wood pulp as a feedstock and would otherwise bypass farm production, turning out fruits and vegetables in cell culture production facilities located in urban centers.[8] Thus, the article suggests, farms and the need for farmland would be rendered obsolete.

Such a futuristic notion is not possible today and may not be for generations, if ever. On the other hand, new crops are already being created through genetic engineering and cell culture propagation. The emergence of such new crops (or livestock), when patented and commercially available, may create new economics for production agriculture, and may have dramatic effects on how farmland will be used and by whom it will be controlled.

If genetic research and development should greatly improve production efficiency per unit of land, then farmland which does not enjoy the application of such new technology may become a relatively less valuable resource. Successful exploitation of farmland may require farmland owners to enter production contracts or otherwise gain access to genetic materials through cooperative action or vertical integration. In effect, productive use of farmland and the consequent benefits of farmland ownership may be shifted to the person who has access to the new technology. Contract rights may become more valuable to producers than land ownership. Of course, if new genetic materials are broadly

available from competing sources, this new technology may have no greater impact on the structure of agricultural production than, say, hybrid seed. However, some observers believe the size of research investments, proprietary restrictions, and possible design of products for specific market niches will cause radical structural shifts.

Lawyers and their agricultural clients must look at farmland ownership and control in the context of the real world – not the world as it existed twenty years ago or as it may exist fifty years in the future – but the world as it exists today and as we reasonably expect it to develop in the years and decades immediately ahead. Innovative lawyers and their clients are not focusing first on traditional legal devices and institutions. They are looking instead at the underlying business and economic objectives, then considering legal constructions governing such traditional ownership elements as possession, control, liability, earnings maximization, earnings distribution, and asset disposition, in order to accomplish the intended objectives. This is an analytical "flip" that is already occurring

Similarly, in structuring land transactions, these analysts and practitioners consider the burdens as well as benefits of farmland ownership, and then decide what parties should bear which burdens or enjoy which benefits. The laws of contract, lease, corporations, trusts, partnerships, equity and debt instruments, and governmental programs, as well as traditional real and personal property law, then may be designed to accomplish the objectives.

Dynamic factors reshaping agriculture and farmland ownership issues

Demographics and new technology are not the only areas of change that promise to restructure agriculture and refashion traditional regimes of land ownership and control. At least four powerful forces of change are apparent:

(1) Financial diversification, in both financial instruments and financial institutions, will create both opportunities for new investors and new investment vehicles in farmland. Successful farmers and others will utilize new financial sources and new financing techniques, such as stratification and securitization of both equity and debt. Creative application of these new tools may be used to accomplish practical goals, such as improving liquidity and flexibility for farmers or spreading portfolio and credit risks while retaining farmer control.

(2) Asset requirements will continue to increase in many areas of production, while new market niches with lower asset requirements may arise in some areas. Those who thrive must accurately judge the optimum size of operation for producing, processing, and marketing their products, and then assemble the necessary talents and management skills, and assimilate the appropriate resources efficiently through application of equity, debt, contractual arrangements, cooperative relationships, and other techniques.

(3) Risks associated with farmland ownership will increase markedly in some areas. Environmental risks will increase with rising popular concern and with regulatory and judicial enforcement, particularly in the areas of chemical waste disposal and groundwater contamination. Other government regulatory risks associated with the operation of farms (rather than the ownership of farmland), such as labor relations, product liability, food safety, and animal rights liability, may also increase. In the absence of more rigorous planning, the traditional list of farmland ownership risks, such as production risk, credit risk, interest rate risk, liquidity risk, portfolio risk, taxation risk, and general liability risk, may also become problematical.

(4) Marketplace trends, such as increasing demand for quality-controlled or process-specific commodities and retained identity products, will make production of generic farm products less profitable. Processing technology may force these trends upon farmers, as the processors of farm products seek efficiencies through more rigorous purchasing requirements for the physical and chemical characteristics of farm products. Genetic developments may make possible the production of highly differentiated products for specific processing requirements, and owners of the proprietary genetic materials that meet key industrial end-user needs will be in a strong position to exercise influence on the farm production. These trends will tend to bring about more value-added production, contract production, forward or backward integration, or all of the above.

Traditional government policies on farmland ownership

Farm legislation in recent years, particularly at the state level, has often focused explicitly on farmland ownership. More than half the states have had laws that restrict farmland ownership by foreigners or corporations.[9] More commonly, at the federal level farm policy has centered on bolstering farm income, improving economic stability in the agricultural sector, enhancing rural development, or responding to catastrophic events. But even when these broader purposes are stated, widely-held objectives of assisting "family farms" often underlie the other goals. Typically, the vision of a "family farm" has been a crop or livestock production enterprise whose land and other assets are owned and operated by a single family in a traditional rural setting.

Even when not expressly intended, farm programs have greatly affected farmland ownership realities, sometimes in ways that probably would not have been approved of by the legislators who created the programs. For example, some commentators have concluded that federal commodity programs have worsened the plight of family farmers by artificially supporting prices, which creates inflated anticipated income streams that are then capitalized into the value of farmland, thus making entry more difficult, distorting investment analysis, and causing farmland values to collapse when such programs are terminated.[10] These results are especially detrimental to beginning, under-capitalized and highly leveraged farmers.

When policy debates have directly addressed farmland ownership policy, the focus usually has been on who owns or should own farmland rather than what elements of ownership are important or desirable. "Ownership" has generally been assumed to be a static concept with desirable attributes such as control over land use, rights to economic benefits from exploiting the land, and disposition rights. New laws have focused on encouragement of ownership by certain demographic groups, such as local family farmers, or more commonly restricting ownership by other groups, such as corporations or foreign interests.[11]

Laws built on such policy foundations have sometimes altered the behavior of affected groups and occasionally have given rise to circumventing legal devices. But despite their controversy,

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whether such laws have had a significant impact on the structure of agriculture is difficult to assess. Because only nine states have restricted corporate ownership of farmland, some observers suggest that corporate investors have simply chosen to operate in other states, bringing their debated mix of economic and social benefits and costs to those states.[12] Practical evidence of the limited economic effect of these laws may be suggested by the fact that no substantial body of case law or significant area of legal practice has emerged in the area.[13]

Restrictive farmland ownership laws based on preferences for "who should own" farmland may continue to be controversial in the 1990's, but their net, national economic effects very likely will be trivial compared to larger trends and developments affecting farmland ownership.

Broader economic policies and trends, both public and private, tend to have much greater weight, and major farm program changes – national and international – also tend to have more impact. For example, policy initiatives affect farmland ownership issues through such objectives as improving access to credit for land financing, easing the financial burdens of first-time entry into farming, stabilizing commodity prices and hence returns on investment and labor, or fostering rural development.[14] One may argue that past policies in these areas either have had their intended effects or instead have contributed to larger problems, such as the agricultural depression or the farm credit crisis of the 1980's. Be that as it may, those policies have had profound influences on who owns farmland and how it is used. Moreover, farm policy objectives are not the exclusive province of the so-called "farm bills." For example, the Tax Reform Act of 1986 evinced a public policy of decreasing investment in agriculture by non-farmers. The new provisions, denying loss deductions to passive investors, were devised, in part, to discourage such investment.[15]

Proposals for broadening equity ownership of farmland

Economists, legal scholars, investment houses, think tanks, and policy analysts of sundry stripes have ventured forth in recent years with new plans, sometimes in elaborate detail, either to protect current farmland ownership patterns or to create new equity relationships. Generally those schemes have not achieved the national prominence that has been anticipated by some and feared by others.

In the late 1970's and early 1980's the primary focus of attention was on investment by nonfarmers who sought to benefit from appreciation of farmland values that was anticipated in those times. The Agland Trust proposal of Chicago's Northern Trust Bank was the most notorious. After a public outcry of concern for the future of family farms and after Congressional hearings, the proposed limited partnership investment was withdrawn. But the idea of institutionalized nonfarmer-investor ownership of farmland inspired continuing debate and undoubtedly contributed to laws in several states to restrict farmland ownership further.[16]

Farmland values in most places, of course, did not continue to appreciate after the early 1980's, causing attention to shift away from restricting capital investment in agriculture toward alleviating the plight of farmers in agriculture's financial crisis and allowing farmers to reap the perceived benefits of new outside sources of equity. Representative of this new perspective is a resolution passed in 1987 by the American Farm Bureau Federation: "We should develop a plan that would assist in the recapitalization of production agriculture in the United States through an equity investment program using both public and private funds."[17]

A summary of three innovative proposals may be useful to put this area of policy formation in the context of planning for the 1990's.[18] In 1986, Professor Neil Harl proposed the creation of a federally funded or hybrid federal-state-private Agriculture Finance Corporation (AFC) to acquire and temporarily hold farmland that would otherwise be lost to farmers through foreclosure, liquidation, or acquisition by lenders.[19]

The proposal was intended to be temporary; farm were to be sold back to farmers when conditions improved. The AFC plan addressed the perceived economic situation of the time, when massive liquidations loomed and investor interest waned. Further depression of prices threatened a widespread collapse of farmland values, which might spiral the economy downward to the potential detriment of farmers, then lenders, and finally the broader economy. If Harl's proposal had worked as hoped, farmland prices would have been bolstered and rental rates would have been established as "reasonable" levels for farmers, through direct federal subsidies. The government would have become an equity investor.

In 1988, University of Illinois Professor Harold Guither and Joseph Bourn, a professional farm manager, advanced the idea of a Cooperative Farmland Ownership System (CFLOS), the stated purposes of which included reducing capital risks associated with land ownership by individual farmers and creating an investment vehicle for both farm and nonfarm investors to diversify their portfolios. The CFLOS would be patterned after the Farm Credit System, with initial federal government ownership being sold over time to corporate, partnership, or cooperative owners of System institutions. "A major difference between the functions of CFLOS and the Farm Credit System, as it has operated through the years, would be the emphasis on equity ownership and professional management rather than debt financing of farm land."[20]

The authors' suggested that opportunities for present farmers to remain in farming would be enhanced by their proposal, because debt-burdened farmers could remain as farm operators of CFLOS land after selling their farms and perhaps purchasing equity shares of a lesser value in CFLOS institutions.[21]

A 1989 paper which expands upon a 1987 treatise by Lance McKinzie, Timothy G. Baker, and Wallace Tyner of Purdue University advocates the creation of a futures market in farmland.[22] Such a futures market would be designed to facilitate hedging contracts and reduce farmland purchase transaction costs and capital risks, particularly for farmers who enter the business during periods in the economic cycle when land prices are high, requiring the assumption of heavy debt burdens. The authors believe their proposal would create stability through both economic cycles and generational transfers and would increase liquidity and therefore efficient resource allocation for both farm and nonfarm investors.[23]

Institutionally, a futures market in farmland could be initiated by creating a large, centrally controlled, diversified portfolio of farmland, on which contracts, options, or other financial instruments might be based, but that would require "vast funding and careful management" and "the government would probably need to be involved."[24] Alternatively, McKinzie proposes an index of land values or financial swaps, with standardization and regulation, as a less expensive start-up method.[25]

The proposals described above deserve to be evaluated separately on the basis of the policies advanced by each and the likelihood of achieving them. They share a characteristic, however, that is common to many other policy proposals on this subject. That is that their implementation is likely to involve elaborate national schemes, requiring federal or extensive state legislation, regulation, and funding. For that reason alone, their adoption is unlikely. To the extent that these proposals attempt to create through legislation new regimes that would be perceived to threaten the family farm, their political acceptance is

(Continued on page 7)

unlikely. The ideal of family owned and operated farms, characterized by traditional fee simple ownership, is too solidly established in the minds of too many political decision makers, and indeed in popular politics. To the extent these proposals would require significant federal or taxpayer funding, their embracement in the near future is even less likely.

Structural reform on a transactional rather than a policy basis

New regimes of farmland ownership are not likely to come from new legislation or the dramatic arrival of new national institutions. Rather such changes, through new equity structures or new control and risk relationships, are far more likely to come from the incremental efforts of innovative businessmen, financial advisers, and lawyers addressing practical problems in specific farm business settings. That is not to say that new legislation or public institutions will not come about, but instead that they are likely to come about piecemeal and be preceded by private sector adaptations on a case-by-case basis to changing economic realities.

Practical farm problems of the 1990's require analysis, reevaluation, and allocation of various aspects of ownership, such as control, transferability, rights to earnings, security, liquidity, and risk management (including such overlapping areas of risk as portfolio, capital, credit, input availability, production, handling, market, and liability risk). Today's farms and farming are vastly different from those of twenty or fifty years ago. They have adapted step by step as our economy, technology, and society have changed. There is no reason to believe that the process is over. Indeed, emerging trends both inside and outside of agriculture are bringing about adaptations day by day. Lawyers and their clients who look under traditional approaches, identify new economic realities, and find new legal solutions will create the "farm flips" that may bring greater opportunity, efficiency, and prosperity to American agriculture.

That brings us back to where we began: innovations in Finance, Asset management, Risk management, and Market orientation ("F-A-R-M") and dynamic interaction among Farmers, Lenders, Investors, Purchasers, and Suppliers ("F-L-I-P-S") offer new perspectives on farmland ownership in the 1990's. Future comments in this series will focus on legal relationships that appear to be emerging from each of these specific areas of transition.

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1 Thompson, *Tomorrow's Land Tenure*, AgriFinance, Nov 1988; for current data see *Agricultural Land Values and Markets, Agricultural Resources: Situation and Outlook Report*, USDA ERS rep. AR-14, at 16, June, 1989 [hereinafter called "Outlook Report"] Thompson, *supra*. at 19.

2. Outlook Report at 16.

3 Thompson, supra note 1, at 19

4 Tweeten, Adjustments in Agriculture and its Infrastructure in the 1990s, Positioning Agriculture for the 1990s, Oct. 1988 at 92, 110 Tweeten has set out the following summary of return to farm assets in 1986:

Farm Sales Class ($1,000/farm)	Current Rate of Return to Farm Assets (%)
500 +	20
250 to 500	9
100 to 250	4
40 to 100	–1
20 to 40	–1
10 to 20	–3
5 to 10	–3
Less than 5	–3
All farms	4

5 McKinzie, To Facilitate Equity Financing in Agriculture, Draft, Purdue Univ., Dept Agric Econ, Dec 12, 1988, at 14.

6 Outlook Report; Tweeten, Are Farmers Predestined to Earn Chronically Low Rates of Return on Resources in the Absence of Government Support Programs, in *Research in Domestic and International Agribusiness Management*, Vol 9 (R Goldberg ed 1989)

7. *See* Duncan, Hard Realities and New Opportunities, Positioning Agriculture for the 1990s, Oct 1988, at 6. *but see* Tweeten, *supra* note 4 at 93

8 The Washington Post, Sept 25, 1989, at A3

9. As of early 1989, nine states banned corporate ownership of farmland and corporate involvement in agricultural production All of those states were contiguous and located primarily in the Great Plains *See* Smart & Hoberg, *Corporate Farming in the Anti-Corporate Farming States*, Nat Ctr Agric L Res Info, 1989; Schian & Seid, *State Laws Relating to the Ownership of U S. Land by Aliens and Business Entities*, USDA ERS Staff Rep No AGES861103, Oct 31, 1986

10 *See, e g*, McKinzie *supra* note 5

11. For a discussion of policy rationales for such laws and a survey of statutes and case law on this subject, *see*, Smart & Hoberg, *supra* note 9

12 *Id*

13 For some interested parties, of course, there have been considerable expenditures on the legal process involving those laws An area where restrictions on farmland ownership have generated case law is foreclosure and land retention rights of corporate lenders *See, e g*, *State v. Liberty National Bank and Trust Co*, 427 N W.2d 307 (N D 1988).

14 A review of policy developments in these areas would embrace virtually all farm legislation over many years, and is beyond the scope of this comment

15 *See*, *General Explanation of the Tax Reform Act of 1986*, H R. 3838, 99th Cong, Pub. L No 990514, Joint Committee on Taxation, Committee Print, May 4, 1987, pp 211-12.

16. For contemporary comments on the AgLand Trust proposal, see *Investors in Farmland are on Dangerous Ground*, Fortune, Jan. 29, 1979 (domestic ed) at 97; *Investing in Rural Land*, Business Week, Apr. 30, 1979, at 106.

17 Guither & Bourn, Equity Investment with Professional Farm Management: Developing an Alternative Policy to Debt Financing of Agricultural Land, paper presented at Am Agric Econ A., July 1988

18 The proposals chosen for presentation here are dissimilar in many respects, including policy objectives and scope of analysis. They are discussed here for the purpose of assisting with a perspective on trends in farmland ownership They do not necessarily correspond or conflict with the policy objectives of the author of this comment For a discussion of these and other proposals, see, McKinzie, Baker & Tyner, A Perspective on U S Farm Problems and Agricultural Policy, 1987; and Guither & Bourn, *supra* note 17

19. N Harl, *A Proposal for Interim Land Ownership and Financing Through an Agricultural Financing Corporation*, 8 J. Tax'n & L. at 19, 1986

20. Guither & Bourn, *supra*, note 17

21. *Id.*

22 McKinzie, Baker & Tyner, *supra*, note 18; McKinzie, supra, note 4

23 Both the book and the paper discuss in depth the effects of nativity and timing on the success of a beginning farmer For example, a farmer who makes his farm investment with debt financing during a depression is likely to succeed, while a farmer who invests during a period of high land prices is likely to fail "When you start makes all the difference" McKinzie, *supra* note 5, at 5 "The fact is that our current system which encourages debt financing does not easily accommodate substantial downward revisions in farm asset values Yet downward revisions must be accommodated." *Id*

24 *Id.* at 25

25 *Id* at 26

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